

Message Text

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ACTION EA-09

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C O N F I D E N T I A L TOKYO 14795

E.O. 11652: GDS

TAGS: EGEN JA

SUBJECT: JAPANESE ECONOMIC SITUATION

SUMMARY: JAPANESE ECONOMY IS STRUGGLING TO GET OUT OF ITS TROUGH, BUT WITHOUT MUCH SUCCESS. INFLATION IS DOWN CLOSE TO ONE DIGIT LEVELS, ALTHOUGH SOME GOVERNMENT CONTROLLED PRICES WILL INCREASE. HOWEVER, CONSUMER AND BUSINESS DEMAND IS WEAK, AND GOVERNMENT SPENDING IS ABOUT LEVEL COMPARED TO EARLY 1975. LDP LEADERS HOPE FOR BUT DO NOT APPEAR CONFIDENT OF A SOLID RECOVERY BEFORE MID-1976. END SUMMARY.

1. THE JAPANESE ECONOMY CONTINUES TO BUMP ALONG NEAR THE BOTTOM OF ITS TROUGH IN SPITE OF WELL-PUBLICIZED EFFORTS TO STRUGGLE OUT. THOSE EFFORTS ARE RATHER HALF-HEARTED, AND A SOLID CONSENSUS ON WHAT TO DO IS LACKING. THE IMPERIAL VISIT, THE ECONOMIC SUMMIT IN NOVEMBER, THE PREPCON II IN PARIS, AND THE FLUCTUATING POLITICAL FORTUNES
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OF PRIME MINISTER MIKI IN THE DIET SEEM TO BE WELCOMED AS USEFUL

DISTRACTION FROM THE ECONOMIC DOLDRUMS.

2. THE OVERALL ECONOMIC SCENE IS IN FACT NOT TERRIBLY BAD. UNEMPLOYMENT AT 1.8 PERCENT IS NOT EITHER A POLITICAL OR ECONOMIC PROBLEM. FEARS OF WIDESPREAD BANKRUPTCIES HAVE NOT BEEN REALIZED. INDUSTRIAL PRODUCTION HAS RECOVERED FROM THE DEEP LOWS OF EARLY THIS YEAR, AND IS APPROXIMATELY STABLE. NEW AUTO REGISTRATIONS ARE UP, BUT TO SOME EXTENT PURCHASES MAY BE IN ANTICIPATION OF HIGHER PRICES WHICH GO INTO EFFECT ON JANUARY 1 ALONG WITH HIGHER ANTI-POLLUTION STANDARDS. HOUSING CONSTRUCTION, THOUGH NOT BOOMING, HAS INCREASED AND IS GETTING GOVERNMENT SUPPORT. EXPORTS ARE DOWN, BUT SO ARE IMPORTS AND THE BALANCE OF PAYMENTS IS NOT A PROBLEM OR A CONSTRAINING FACTOR ON DOMESTIC ECONOMIC POLICY.

3. THUS JAPAN IS A LONG WAY FROM A SERIOUS CRISIS. THE PROBLEM REALLY IS HOW TO RESTORE PROSPERITY AT THE SIX-SEVEN PERCENT GROWTH RATE LEVELS MOST OBSERVERS NOW CALCULATE AS REASONABLE FOR JAPAN. THE FUNDAMENTAL STRENGTH OF THE ECONOMY IS UNIMPAIRED AND ITS STRUCTURE IS FLEXIBLE ENOUGH TO MEET SHIFTING SUPPLY AND DEMAND SITUATIONS. INFLATION, EVEN THOUGH STILL RUNNING AT OVER TEN PERCENT, IS NOT A CONSTRAINT. SOME GOVERNMENT CONTROLLED PRICES WILL HAVE TO BE INCREASED SOON WITH AN ACCOMPANYING IMPACT ON THE PRICE INDEXES, BUT THE GOVERNMENT DEFICIT WILL GO DOWN CORRESPONDINGLY. THE WEAKNESS IS IN AGGREGATE DEMAND.

4. IN NORMAL TIMES, WHICH UNTIL RECENTLY MEANT TIMES WHEN GROWTH HAS BEEN ABOUT TEN PERCENT, THE ECONOMY HAS BEEN PULLED ALONG BY STRONG DEMAND FROM CONSUMERS, INVESTORS AND EXPORTERS. AT PRESENT ALL THREE ARE SLACK. THE JAPANESE HOPE EXPORT DEMAND WILL IMPROVE AND ARE LOOKING FOR A BOOST, BOTH ACTUAL AND PSYCHOLOGICAL, FROM U.S. RECOVERY, EVEN THOUGH THE EFFECT IN REAL TERMS WOULD BE MODEST COMPARED TO WHAT IS NEEDED. BUSINESS INVESTMENT IS VERY SLOW AT PRESENT AND WILL NOT RECOVER UNTIL AFTER OVERALL MARKET DEMAND AND THE RATE OF RETURN ON NEW CAPITAL HAVE INCREASED SIGNIFICANTLY. THE JAPANESE CONSUMER IS MOSTLY A MYSTERY TO ECONOMIC PLANNERS WHO CONFESS THAT THEY HAVE FEW TOOLS TO MEASURE HIS BEHAVIOR, LET ALONE HIS INTENTIONS. HOWEVER, HE APPARENTLY REMAINS IN A CONFIDENTIAL

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CONSERVATIVE MOOD. CONSUMER SAVINGS RATES, NORMALLY A HIGH TWENTY-TWO TO TWENTY-FOUR PERCENT IN JAPAN, HAVE RISEN TO TWENTY-FIVE TO TWENTY-SIX PERCENT AS BUYERS HOLD BACK LIQUIDITY OUT OF CONCERN FOR HARDER TIMES AHEAD. THE DIFFERENCE IN SAVINGS RATES SEEMS SMALL, BUT IT IS HUGE WHEN TRANSLATED INTO TOTAL DEMAND IN YEN TERMS. EVERYONE IS HOPING AND MANY ARE EXPECTING THAT CONSUMER SPENDING WILL REVIVE, BUT NO ONE HAS PRODUCED

EVIDENCE THAT IT WILL.

5. ONLY GOVERNMENT SPENDING IS LEFT. THE MUCH TOUTED FOURTH RECOVERY PLAN WILL KEEP GOVERNMENT SPENDING FLOWS FROM DROPPING, BUT WILL NOT ADD ANYTHING NEW. TAX CUTS HAVE NOT BEEN PROPOSED AND FINANCE MINISTRY OFFICIALS STRONGLY OPPOSE THEM AS LONG AS BUDGET DEFICITS EXIST. DEPUTY PRIME MINISTER FUKUDA IS ALSO ADHERING STOLIDLY TO HIS CONSERVATIVE LINE, YIELDING ONLY BY INCHES TO PRESSURES FROM BUSINESS FOR MORE INJECTIONS OF CREDIT AND GOVERNMENT SPENDING.

6. ECONOMIC RECOVERY IN JAPAN IS STILL SLOW. WE WOULD AGREE WITH THE OECD SECRETARIAT ASSESSMENT, PARTICULARLY ITS UNEMPLOYMENT ESTIMATES (OECD PARIS 26507, PARA 7), EXCEPT FOR THE KEY DIFFERENCE THAT "BOUYANT PRIVATE CONSUMPTION" IS NOT EVIDENT. THE OFFICIAL GOP FY 1975 GROWTH PROJECTION WAS RECENTLY SCALED DOWN FROM 4.3 PERCENT TO ONLY 2.2 PERCENT. OUR EXPECTATION IS FOR NO CRISIS BUT, UNLESS A POLITICAL DECISION IS MADE TO SPEED UP THE PACE OF RECOVERY THROUGH STRONG MEASURES, SIGNIFICANT ACCELERATION IS UNLIKELY.
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